FOLLOW-UP QUESTIONS ON PROPOSED PRICING AND COST RECOVERY FOR GRID WEST

SECTION A – QUESTIONS AND ANSWERS FROM PRICING SEMINAR

Topic: Pricing for and Revenues from Grid West AFC Sales and Released Rights

(1) **Question:** How will the revenues generated from AFC sales be tracked? Also, how will the revenues generated by AFC sales by Grid West be distinguished from revenues generated by the sale of transmission customers' released[1] rights?

Answer: Grid West will be able to track revenues from AFC (Available Flow Capability) sales and distinguish those revenues from transmission customers' offers of rights into the Grid West reconfiguration service market (RCS).

Injection-Withdrawal Rights (IWRs) obtained through RCS will be sold at the clearing prices established through the auction process. Those buying IWRs in the RCS will pay the clearing price, which is the difference between the relevant scheduling points. Transmission customers offering rights will receive the difference in clearing prices for the relevant scheduling points.[2]

The locations and amounts of the rights offered into the RCS by transmission customers will be known, and the offered rights will be sold only if the clearing prices meet or exceed any minimum price specified by the selling transmission customer. Grid West will offer AFC at the same time, and the capacity offered by Grid West will be priced and sold in exactly the same manner as rights offered by transmission customers.[3] Grid West will be a price taker and its share of the combined revenues from sales of AFC and transmission customers' rights will be the net derived by subtracting revenues owed to transmission customers offering rights from total RCS revenue.

(2) **Question:** Will all revenues resulting from the release of AFC by transmission customers be credited to those who release rights to that capacity? And the converse, will all revenues resulting from the release of AFC by Grid West (e.g., "found AFC") be credited to the "communal bucket"? Following this logic, is the expectation that the

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[1] Although questioners used the term "released rights," the appropriate term used by TSLG is offered rights. There will also be *releases* of flexibility contained in network service rights that will be a part of the auction process.

[2] For further discussion of pricing for IWRs through the Grid West reconfiguration service auctions, please refer to the TSLG white paper, *Transmission Rights Reconfiguration Service,* which is posted on the Grid West Website at www.gridwest.org/Doc/P2-TSLG-Papers_Release-Drafts_12May05-2.pdf.

[3] For further discussion of the Grid West reconfiguration service auctions, please refer to *Transmission Rights Reconfiguration Service* (*see* preceding footnote).

potential $50 million loss of short-term/nonfirm transaction revenue (see page 8 of the Pricing and Cost Recovery White paper) is expected to be made up with sales by Grid West?

<u>Answer</u>: Yes, to the first two of these questions. As to the third question, the Pricing Work Group does not have an expectation about how much of the $100 million of 2003 short-term and non-firm sales revenue will be made up through AFC sales in the RCS. Many Pricing Work Group members expect that AFC sales will generate significant revenue, but it would be more or less than what Grid West transmission owners, in the aggregate, earned in 2003. The $50 million figure was meant as an example based on what the Pricing Work Group considered to be a conservative assumption that the RCS would generate at least half of what transmission owners generated in 2003. Grid West may have to implement a revenue replacement charge to recover some of these revenues if the revenues generated from new service supported by AFC (both RCS and long-term requests) are not enough.

(3) **<u>Question</u>:** Who gets the revenues from sales of AFC, both that released by transmission customers and that released by Grid West?

<u>Answer</u>: Technically, transmission customers do not "release" AFC, they offer their rights. Grid West offers AFC. For a discussion of how the revenues are distinguished (those due to transmission customers versus those due to Grid West), see the answers to Questions 1 and 2. Note also (as explained in Section 5 of the pricing white paper) that the revenues Grid West earns from AFC sales are subsequently allocated to the transmission owners.

(4) **<u>Question</u>:** What will be the price that is awarded for IWRs?

<u>Answer</u>: With respect to short-term IWRs purchased in the Grid West reconfiguration service auctions, the pricing mechanism is described in the answer to Question 1. With respect to long-term IWRs, pricing would be determined through one of the four long-term pricing options proposed by the Pricing Work Group (for IWRs that can be granted from AFC) or according to FERC's "or" pricing policy (for IWRs that require system upgrades or expansion).

(5) **<u>Question</u>:** In defining a "single" system, especially for network service, will a Consolidated Control Area (CCA) be considered a "single" system? If not, pancaking may continue to limit transactions within the CCA as well as throughout the Grid West footprint.

<u>Answer</u>: The Pricing Work Group did not assume that control area consolidation would determine how transmission owners' systems are defined for rate-setting purposes. Discussions of control area consolidation have been grounded in operational considerations, rather than pricing objectives. Even with consolidation, the Pricing Work Group assumed that a system (for purposes of applying a company rate structure) would be defined in terms of asset ownership or contract rights. In other words, no matter how many control areas consolidate, we will still need to work through what constitutes a "single system" if needed for rate-setting purposes.

The Pricing Work Group has conferred with the TSLG (to a limited degree) on the proposed scope of new network service. The approach that the Pricing Work Group proposes is an attempt to balance the tension between eliminating pancakes and managing capacity commitments to serve network transactions. The work group was unsure about how much future demand there would be for entirely new network service (given that all load on the system is currently being served and in most cases existing network rights would also cover load growth). Given that Grid West operation will be phased in over time, the Pricing Work Group did not see this issue as a first priority but it is a good subject for further discussion. There was a general agreement by the Pricing Work Group and the TSLG that for now, the proposal should be to limit network service to a customer's "host" system, and the concept of host system is not affected by control area consolidation. But both groups acknowledge the need for further consideration, given some parties' concerns that those using network service might pay a rate "pancake" if they need rights to integrate resources outside the host system.

(6) **Question:** Did the Pricing Work Group consider a pricing scheme that is based upon the average of the points of injection/withdrawal? And if so, why was that found unattractive?

Answer: The Pricing Work Group considered this approach and concluded initially that pricing service at the Grid West system-wide average rate would be simpler. The Pricing Work Group is willing to note this suggestion as another possible variation on cost-based rates for new long-term service.

(7) **Question:** Will obtaining IWRs in the long-term market impact the availability of IWRs in the short-term market?

Answer: Yes, just as is the case today. Short-term service is provided from capacity remaining after satisfying long-term commitments. It is also likely, however, that parties holding long-term rights (either certified pre-existing rights or long-term IWRs purchased from Grid West) will offer portions of those rights into the RCS from time to time.

(8) **Question:** Does legacy service have any impact on the new service determination?

Answer: If this question is intended to address whether a party must have existing rights to request new service, or whether its existing rights would be factored into determinations concerning Grid West's ability to grant new service to that customer, then the answer is no. New service will be offered to any eligible customer (whether the customer needs new service to supplement its legacy service or the customer has no pre-existing service rights).

Also, the company rate that would apply to new service would not be affected by whether the customer requesting new service did nor did not have legacy rights. Rather, the applicable company rate would be determined by whatever pricing principles governed new service for all parties (such as locations of the requested injection and withdrawal points or some form of auction or system-wide average rate, depending on what approach the Grid West Developmental Board adopts).

If this question is intended to address whether Grid West considers legacy commitments in general before determining whether it can satisfy requests for new service, then the answer is yes. Grid West will sell new service from capacity (AFC) it determines is available only *after* factoring in all the demands on the system associated with legacy service.

(9) **Question:** Please explain the auction options more.

Answer: The auction proposal is intended to provide pricing continuity between the short-term (RCS) market and the long-term market. Also, because an auction is not limited by cost-based rates, it may generate more or less revenue than the cost-based options proposed. If the auction produces more revenue than cost-based options, this would reduce the need for replacement revenues, while a lower level of revenues would increase the need for replacement revenues. The Pricing Work Group recognizes that the auction concept is the least-tested alternative and is a significant departure from the pricing mechanisms that transmission owners have used to date.

The auction mechanism could be designed a number of different ways. The white paper suggests three for consideration: (1) the auction could be an extension of the RCS so that multi-year rights, such as 5-year, 4-year, 3-year, 2-year, and 1-year IWR pairs, could be offered sequentially with the highest bidder being awarded the capacity; (2) the auction could be triggered by the request for long-term service, e.g., the request would trigger a competition for the desired capacity and the highest net present value would determine the winner; and (3) the auction could be formulated around an open season concept, where specific rights could be offered for bid and the highest net present value bid would determine the winner.

(10) **Question:** Has the Pricing Work Group described the basis of rates, but not the basis of payments?

Answer: The Pricing Work Group has addressed both. The pricing white paper presents several options for pricing new long-term service (Section 4), and Section 5 of the white paper discusses how Grid West revenues from selling new long-term and new short-term service will be allocated to the transmission owners.

Topic: Lost Revenues and Replacement Revenues

(11) **Question:** The example in the white paper and in the slides indicates that of $1.8 billion in total revenue requirement about $100 million of short-term/nonfirm transactions is potentially lost revenue. How will that loss be allocated among the transmission owners?

Also, please indicate to what extent each of the transmission owners stands to lose revenue from long-term as well as short-term/nonfirm losses.

Answer: The figure of $100 million in the slides was derived by adding the non-firm and short-term sales revenues (for 2003) of each of the transmission owners.[4] So, the amount of the $100 million attributable to each transmission owner is known. The spreadsheets from which the Pricing Work Group developed its estimates are posted on the Grid West Website.[5] Once Grid West begins operation, it will be the sole provider of new short-term transmission service (through AFC sales in the RCS). Revenues Grid West earns from the RCS, as well as from sales of long-term IWRs that can be granted from AFC, will be allocated to the transmission owners based on relative "need." Need in this context will be determined according to how much revenue has been "lost" by each transmission owner due to Grid West implementation. Lost revenue will include revenues previously derived from short-term and non-firm transmission sales, as well as revenues associated with discontinued long-term contracts (to the extent the discontinuation is attributable to Grid West offering a more attractive "replacement" service, as opposed to an instance in which the transmission customer no longer requires transmission service at all, because this latter case is a loss of revenue that would have occurred even in the absence of Grid West; in other words, an ordinary business risk).

The Pricing Work Group has discussed at a high level how well it can judge risk of lost revenue associated with long-term transmission service agreements. This issue raises multiple questions, however. The first is: How much revenue is associated with existing long-term agreements that will expire during the period in which the "company rate approach" is in effect? The second question is: Out of those expiring contracts, how many will be with parties other than transmission owners? (This is because most long-term agreements between transmission owners will be subject to a "mandatory rollover" provision even if they otherwise would have expired.) The third question is: Out of contracts with non-transmission owners that *could* be allowed to expire, how many *will* be allowed to expire?

It is this third question, in particular, that introduces the most uncertainty. In a situation in which all schedules must have accompanying physical rights, it follows that those holding pre-existing rights needed for load service would not be inclined to give them up unless they are confident that they can re-obtain the necessary rights and that new rights would provide more favorable terms. The TSLG and others have generally recognized that in most areas, the existing system is heavily subscribed and additional long-term requests are already queued up, waiting to be granted. If an existing rights holder allowed its current rights to expire, the resulting capacity could very well be used to grant other parties' existing requests and would not be available to the customer that allowed

[4] Please note that while the nonfirm and short-term sales revenues were updated to reflect actual transactions in 2003, not all data in the spreadsheet were updated. If there is a decision to continue work on Grid West beyond Decision Point 2, this could include further refinement of these data and evaluation of their implications.

[5] www.gridwest.org/Doc/GW_PWG_UpdatedData_Feb102005.pdf

its rights to that capacity to expire. This probability might even increase under a flow-based methodology, because the capacity released on one part of the system may enable the grant of rights on an entirely different part of the system (and so the released capacity would not just be subject to requests for rights on the same transmission owner's system, but also requests for rights on other transmission owners' systems as well).

Although the pricing spreadsheet gives a general sense of revenues associated with long-term contracts, it contains no information about contract expiration dates and it does not distinguish among contracts that are likely to be needed for load service as opposed to contracts associated with power sales contracts or other uses that might give the rights holder more flexibility concerning whether to retain or discontinue rights under these contracts as they expire. The question of whether Grid West will collect more or less revenue for rights than would have been collected if transmission owners had sold the rights under today's rates (both long-term and short-term) is an open one. The Grid West pricing proposal does, however, include a proposal to make replacement revenues available to transmission owners to the extent that they have remaining lost revenues after receiving their allocations of Grid West's AFC sales revenues.

(12) **Question:** Will it be easy to determine what revenue losses result from Grid West implementation?

Answer: The Pricing Work Group does not expect that this will be "easy," but it should be possible to make a reasonable analysis. As explained in the answer to Question 11, it will be possible to clearly determine revenues transmission owners received in the past from sales of short-term and non-firm transmission service, although the Pricing Work Group does not necessarily intend that revenues associated with short-term and non-firm sales in a particular year would be used indefinitely as the basis for future recognition of lost revenues.

It may be less clear with respect to long-term contract expirations whether the resulting revenue loss was due to Grid West implementation, but an important indicator will be whether the customer that previously took service under the expired contract seeks the same or very similar service from Grid West. The Pricing Work Group intends the concept of lost revenues to cover both revenues lost due to discontinued short-term and non-firm sales and revenues lost from long-term contract expirations (other than those that fall into the category of a transmission owner's normal business risk—that is, revenue losses that would have occurred in the absence of Grid West.) The inclusion of revenue losses related to long-term contract expiration means that lost revenue calculations will need to be updated over time.

(13) **Question:** Will Grid West determine lost revenue for each transmission owner?

Answer: The process through which each transmission owner's lost revenues are determined has not yet been spelled out. It is reasonable to assume that both Grid West and the transmission owners will need to agree on how this process will work and how any resulting disagreements will be resolved.

(14) **<u>Question</u>:** Will a determination of lost revenues be subject to dispute resolution?

<u>Answer</u>: The Pricing Work Group has not discussed this issue.

(15) **<u>Question</u>:** Does the Pricing Work Group think that there is an issue in terms of revenue recovery driven by an inability to sell capacity? Isn't the expectation that the capacity that is sold today will be sold tomorrow?

<u>Answer</u>: The Pricing Work Group does expect that capacity that is sold today will be sold tomorrow, but the prices may not be the same. It is therefore possible that there will be under-recovery of revenue if the same capacity sells at lower prices. Short-term IWR prices will be determined through the Grid West reconfiguration service auctions. The Pricing Work Group did not have any basis to compare how reconfiguration auction prices may differ from current charges for short-term and non-firm service. With respect to long-term IWRs, revenue derived from new service is likely to be less in the aggregate to the extent that service that previously required rights on several transmission owners' system (pancakes) can be purchased from Grid West for a single rate.

(16) **<u>Question</u>:** If long-term rights are granted because AFC is available, are the transmission owners in the "middle" of the transaction suffering a revenue loss?

<u>Answer</u>: The Pricing Work Group has not necessarily assumed a loss for any particular transmission owner. The revenues generated by AFC sales will be allocated among all of the transmission owners based on "need" (share of total lost revenues).

(17) **<u>Question</u>:** Do lost revenues exist only until a transmission owner files its next case?

<u>Answer</u>: The Pricing Work Group has not addressed lost revenues in this level of detail. The Pricing Work Group did not assume that the concept of lost revenues would be extinguished as soon as a transmission owner files for updated rates. As explained in the answer to Question 12, the Pricing Work Group's concept of lost revenues encompasses revenue decreases due to long-term contract expiration as well as lost revenues related to discontinued short-term and non-firm service. This means that lost revenues may increase over time as long-term contracts expire, and it also means that lost revenue calculations will have to be updated over time. The Pricing Work Group has not specified how these updating calculations should be made. This will be an important area for future work.

The Pricing Work Group recognizes that it will be important to synchronize the rate setting-determinations with refunds, regulatory changes, etc. The Pricing Work Group has also discussed the possibility that Grid West could establish a reserve to provide some financial "cushion" before it would need to implement rate adjustments or replacement revenue charges.

(18) **<u>Question</u>:** In the evaluation of revenue losses that a transmission owner experiences as a result of implementing Grid West, will revenue gains that result from the implementation of Grid West also be considered?

<u>Answer</u>: The Pricing Work Group has considered this only with respect to how surplus revenues might be allocated if Grid West's AFC sales (both long-term and short-term) produce more than enough revenue to offset transmission owners' "lost" revenues. (See Section 5 of the pricing white paper.) The Pricing Work Group's proposal addresses the need to evaluate revenue losses that result from implementing Grid West, but it did not discuss the implications of any net revenue gains that may result from Grid West. Going forward, it may be appropriate to consider both losses and gains that result from implementing a different market design, pricing scheme, etc.

(19) **<u>Question</u>:** Was the replacement revenue mechanism designed to deal with regulatory lag?

<u>Answer</u>: No. While the Pricing Work Group is concerned about regulatory lag, replacement revenues are intended to address only revenue losses resulting from the implementation of Grid West.

(20) **<u>Question</u>:** Would the charge needed to support replacement revenues be applied going forward?

<u>Answer</u>: Yes. The Pricing Work Group thinks that all market participants should know, in advance, what they will pay to carry out any given transaction. The Pricing Work Group proposes that if Grid West determines that it must collect replacement revenues, the charges would be applied to transactions that take place *after* the determination.

Topic: Development of Company Rates

(21) **<u>Question</u>:** Will the details of what constitutes a company rate be determined by each of the transmission owners?

<u>Answer</u>: Yes.

(22) **<u>Question</u>:** What will the treatment be of the Southern Intertie on the BPA system or how will BPA's company rate be defined?

<u>Answer</u>: Each transmission owner will define its own company rate or company rates in keeping with its own rate-making process. The Pricing Work Group has not prescribed how company rates will be determined, *e.g.*, which facilities will/will not be included, what billing determinants should be used, whether transmission owners will/will not retain segmentation, etc. In the case of BPA, as well as other transmission owners, the Pricing Work Group believes that it should be up to the transmission owner whether segmentation should or should not remain in place. (For BPA, the current segmentation is Network, Southern Intertie, and Montana Intertie.) The long-term IWR pricing proposals are silent with respect to whether the "points of injection" or "points of withdrawal" will reflect segmented company rates. The Pricing Work Group has not explored whether it would be possible to retain segmentation within the structure of "Option 3" (combination of single-system and system-wide average rates).

(23) **Question:** Has BPA considered having more that one company rate; in other words has BPA ruled out the possibility that it might have a separate charge for the Intertie?

Answer: See answer to Question 22. Neither BPA nor the Pricing Work Group has ruled out the possibility that a transmission owner may have more than one company rate.

Topic: Legacy Service and Legacy Revenues

(24) **Question:** Throughout the white paper, *e.g.*, footnote 10, there is a distinction between wheeling that is required for load service and other wheeling. This distinction is important as it implies that wheeling used for load service is expected to remain in place – both rights and payments will continue for the term of the arrangement and will be subject to a "mandatory rollover" for the period of time in which the company rate approach is in effect. What is meant by "load service obligations"? Does this apply to merchant transactions?

Answer: The use of the term "load service obligations" in this context is meant to refer to transmission owners' or customers' obligation to make power continuously available to its firm retail loads (*e.g.*, to meet transmission service obligations to serve native load or to serve customers with load service obligations). Among transmission owners, there are many long-term wheeling arrangements that allow the transmission owner that is taking the transmission service to meet its native load service obligations. For example, a number of transmission owners take transmission service on BPA's system to integrate resources at the mid-Columbia or Colstrip for their native load service, and this kind of use would be tied to "load service obligations." BPA's use of GTA service on other transmission owners' system would be another example. The variety of arrangements reflects different corporate configurations and different legal and regulatory structures. To the extent other types of transmission customers (not transmission owners) also rely on wheeling or network service from Grid West transmission owners to meet their load service obligations, the Pricing Work Group would also expect these arrangements (and associated payment to transmission owners) to remain in place.

In general, the Pricing Work Group has not thought of wholesale transactions in the market as "load service," at least with respect to transactions that have specific terms and no legal obligation to continue service beyond the term of a particular sales agreement.

(25) **Question:** Do the "load service obligations" include OATT service from BPA?

Answer: The simple answer is yes. Current BPA transmission policy is to provide service under the OATT, whether for firm federal power sales or wheeling of non-federal generation resources. The bulk of these services are provided to investor-owned utilities and publicly owned utility customers for the primary purpose of serving retail load. To the extent that customers taking service from BPA rely on OATT service (either network or point-to-point) to serve retail load, the Pricing Work Group viewed these arrangements as associated with "load service obligations." As a result, the Pricing Work Group concluded that these transmission needs would continue through the company rate period.

In contrast, the Pricing Work Group generally viewed wholesale transactions in the market as distinct from "load service," at least for transactions that have specific terms and no legal obligation to continue service beyond the term of a particular sales agreement. (See the answer to Question 24.)

(26) **Question:** Would the rules for these concepts ("mandatory rollover") be dealt with in the Transmission Agreement?

Answer: Yes. The Pricing Work Group has viewed the "mandatory rollover" as essentially a transmission owner's agreement ahead of time that it will exercise its rollover rights under an existing long-term agreement with another transmission owner when the rollover window occurs during the company rate period. This advance agreement to exercise rollover rights would be spelled out in the Transmission Agreement, including any details concerning potential exceptions to the general rules of mandatory rollover. (For example, if a transmission owner has been using another transmission owner's system to make deliveries under a power sales agreement that expires, the transmission service needed for that discontinued sales arrangement would not be subject to the mandatory rollover requirement.)

Topic: System Upgrades and Expansion

(27) **Question:** Who will pay if expansion or upgrades are required? How will benefits and costs be allocated and will this process be triggered by a request for service?

Answer: The Pricing Work Group expects that the transmission customer requesting capacity that is not available will trigger the need for system impact and facilities studies, much as today. Proceeding with a request will commit the requesting party to pay for some or all of the resulting investment. Grid West would be responsible for expansion or upgrade studies, and would consider both wires and non-wires options and evaluate the benefits and allocate costs accordingly. It may be that the investment Grid West recommends in response to a service request creates capacity beyond what is needed to meet the request. This could trigger a process to allocate some costs to others that benefit from the investment.

(28) **Question:** If there is a decision to invest in transmission expansions/upgrades, is it possible that there will be more capacity than needed to meet new service requests?

Answer: Yes. See the answer to Question 27.

(29) **<u>Question</u>:** Has the group talked about the funding process that will be needed for the investment in new lines and what the customer gets?

<u>Answer</u>: The Pricing Work Group has had very little discussion on this topic, but this issue seems to involve planning and expansion procedures as well as pricing arrangements. The planning and expansion effort will be used to assess need, potential solutions, benefits from investment, and costs. The pricing arrangements will need to address the financial transaction, the rates that are developed to recover investment, etc.

(30) **<u>Question</u>:** How do we deal with needed expansion on parts of the system that do not encompass either the injection or withdrawal point?

<u>Answer</u>: The location of the expansion does not need to be tied to requested injection and withdrawal points. To the extent that expansion is needed to satisfy a request for new long-term service, the associated costs and the provision of construction revenue will be tied to whatever part(s) of the system need to be expanded. The process to pay for expansion will be the same no matter where on the system it occurs. See the answer to Question 29.

Topic: Grid Management Charge

(31) **<u>Question</u>:** Did you consider applying the Grid Management Charge on a transaction, *e.g.*, a per-schedule charge, rather than MW-hours?

<u>Answer</u>: Yes, the Pricing Work Group considered this and concluded that charging by MW-hour would result in heavier users paying more of Grid West's operating and development costs. The Pricing Work Group felt that recovering all of Grid West's operating costs through a flat per-schedule fee would result in disproportionate charges to smaller users of the system and intermittent resources, such as wind.

The Pricing Work Group has not yet discussed the details of identifying specific cost elements within the Grid Management Charge and whether some cost elements (such as costs directly related to administering the scheduling process) should be recovered through a different billing determinant (such as a per-schedule fee) than that used for the basic Grid Management Charge. This may be a good area for further discussions.

(32) **<u>Question</u>:** Do you anticipate that other administrative costs, such as dispute resolution, litigation, etc. would be included in the Grid Management Charge?

<u>Answer</u>: Yes.

(33) **<u>Question</u>:** Did the Pricing Work Group consider allocating any excess revenues against the Grid Management Charge?

<u>Answer</u>: The Pricing Work Group considered this approach but a number of members felt that it was very important to maintain clear distinctions between costs related to Grid

West's operating and development expenses and costs related to transmission owners' revenue requirements. This issue could be further considered, however.

Topic: Further Work on Pricing and Cost Recovery

(34) **Question:** Where do we go next with this work product?

Answer: This topic was raised at the June 24 RRG meeting. The expectation is that a synthesis of the pricing proposals, possibly with some discussion of RRG feedback, would be included in a comprehensive package that describes all elements of the Grid West proposal (market and operations design, pricing, risk/reward, etc.). This package was posted on July 22, 2005.

(35) **Question:** With respect to the development of this proposal, how can we influence the proposed design? For example, how can we comment on pancaked rates, *e.g.*, charges for exports and through/out transactions?

Answer: The Pricing Work Group has welcomed comments at the pricing seminar (held on June 23, 2005) and at the RRG meeting held the next day (June 24, 2005). Also, there will be further opportunities for interested parties to comment on pricing (and other aspects of the Grid West proposal package) during the August and September 2005 regional comment period. If Grid West development continues after Decision Point 2 (scheduled for fall 2005), the independent Grid West Developmental Board will have an obligation (under the Grid West Developmental Bylaws) to consult with the RRG, Grid West members, and regional regulators in connection with any proposals it adopts or develops.

SECTION B – ANSWERS TO WRITTEN QUESTIONS

(Note: References in questions are to page numbers and footnotes in the pricing white paper.)

Section B.1 – Questions from Lon Peters

(1) **Statement:** The risk of FERC rejection of "mandatory rollover" of pre-existing transmission contracts between PTOs should be acknowledged, in light of decisions regarding MISO last year (regarding "grandfathered contracts").

Response: The Pricing Work Group considers this to be a legal question that falls outside of its work scope. While there may be some risk, it is important to remember several things. First, the relevant facts and circumstances of the cases are quite different. The MISO has sought FERC recognition as an RTO, and therefore it must satisfy FERC's criteria for RTO status. Grid West does not intend to seek RTO status. Moreover, the MISO proposal requires reformatting physical rights to create standardized FTRs. The Grid West proposal is a simple extension of the existing physical rights model, likely filed under Order No. 888. When filings related to Grid West implementation are submitted to FERC, the filings will request explicit approval of the "mandatory rollover" provision. Furthermore, "mandatory rollover" is just shorthand for an arrangement under which transmission owners agree in advance that, when the rollover window occurs, the transmission owner receiving service will exercise its rollover rights (which it would have been entitled to do anyway).

(2) **Question:** What is the basis for the "conservative assumption" that one-half of the short-term and non-firm revenues are "at risk" in the reconfiguration service (p. 8)?

Answer: Under Grid West, every schedule must be accompanied by a corresponding physical right, as is the case today. Because transmission customers today purchase short term and non-firm rights, it is reasonable to expect that customers will engage in the transactions that require these rights in the future. The Grid West proposal provides for short-term rights (IWRs) to be acquired from the reconfiguration market. One could reasonably posit that buyers will be willing to pay at least as much for these rights in the future as they do today (and perhaps more). The Pricing Work Group chose to cut the present revenues by half to acknowledge that with the switch to an auction mechanism, the revenue could potentially be less. This choice to assume a drop in prices *and* the loss of half of the revenues is conservative in comparison to a plausible but more aggressive view that future revenues will be the same or more.

(3) **Question:** Is it possible to evaluate the risk of customers switching to long-term Grid West service in order to reduce their transmission costs? If it is assumed or determined that this risk is small in the context of the Grid West pricing model, then the white paper should say so.

Answer: The white paper expresses the Pricing Work Group's expectation that the primary risk associated with the loss of long-term transactions is isolated to

NorthWestern's system, which has a number of one-year term transactions with marketers (See pages 7-9). Because the Grid West model is a physical rights-based model and users of the system must secure rights to schedule transactions, the Pricing Work Group believes that most customers will maintain existing rights rather than put rights and use of the transmission system at risk. Also, most revenue associated with long-term wheeling agreements (looking at Grid West's transmission owners in the aggregate) involves service between the transmission owners, which will be subject to the "mandatory roll-over" requirement.

(4) **Question:** Is it consistent with current FERC pricing policy for transmission owners to include in their transmission rates payments made for wheeling on the systems of other transmission owners (footnote 11)?

Answer: Wheeling costs are not typically included in wheeling rates charged for wholesale transactions. The Pricing Work Group did not prescribe how transmission owners would calculate their company rates.

(5) **Question:** Is it clear what "load service" means in the context of "mandatory rollover" (p. 12)?

Answer: See the answer to Pricing Seminar Question 24 (Section A).

(6) **Question:** Is it possible for Grid West to issue a new IWR that would not violate operational criteria but would violate pre-existing transmission rights (p. 14)?

Answer: No. See the TSLG's white papers, "Rights Data Management" and "Transmission Rights Reconfiguration Service."

(7) **Question:** Are there any upper price limits in the RCS auction? If not, does the RCS auction comply with existing FERC policy regarding the reselling of unneeded transmission service?

Answer: The TSLG has not proposed price limits on the RCS auction. When filings are submitted to FERC to implement the Grid West proposal (tariff filings, etc.), the filings will include requests for FERC to authorize a deviation from current OATT resale standards. The approach proposed for the RCS would be consistent with the general policy taken for auctions of financial rights for RTOs operating in the eastern United States.

(8) **Question:** Is there any plan or recommendation that the RCS auction be tested in a limited fashion before full implementation?

Answer: This question is probably one for the TSLG rather than for the Pricing Work Group. The Pricing Work Group believes that it is reasonable to assume that there will be detailed testing of the RCS and other Grid West basic features before Grid West launches commercial operations. Plans for how to test and phase in market and operations features will be developed during the work on Layers 3 and 4 of the Grid West proposal.

(9) **<u>Question</u>:** What is the basis for constraining prices in the IWR auction of new rights so that they cannot fall below a floor (footnote 26)? What would be the basis for such a floor? Would the floor be determined by a long-run analysis? Would the floor apply to both short-term and long-term new rights? Would the long-term, value-based floor apply to short-term auctions?

<u>Answer</u>: All details regarding the specifics of an auction option will be developed in further work after Decision Point 2. The purpose of the white paper is to describe possible options, and the brief discussion of possible floor prices was to acknowledge concerns that had been raised by some members of the Pricing Work Group about a minimum price that would have to be paid to secure transmission capacity through an auction mechanism. Further detail will be needed to support the ultimate choice among these options, which will mean a full understanding of the merits of or problems with an auction floor.

(10) **<u>Question</u>:** What is the basis for the ranking of potential revenues from the four options (p. 22)?

<u>Answer</u>: The ranking of the four options was intended describe some of the discussions concerning qualitative assessments that took place in the Pricing Work Group.

(11) **<u>Question</u>:** Are revisions of the Operational Bylaws required for Options 2-4 (p. 23)? If so, what are the plans for examining potential revisions?

<u>Answer</u>: As the paper indicates, the Pricing Work Group concluded that the Grid West Operational Bylaws might need to be amended to allow some of the pricing options to be implemented. The Pricing Work Group also alerted the RRG to this possibility months before the pricing white paper was posted. The Pricing Work Group believes that if a pricing option has sufficient merit and support from the region, then the Grid West Board and members may be willing to support appropriate revisions to the Bylaws. The Pricing Work Group has not addressed any potential revisions, but these could be considered in connection with work after Decision Point 2 as part of a complete package that includes implementation proposals and suggested Bylaws revisions if warranted.

(12) **<u>Question</u>:** Does the pricing framework assume that BPA will shift from fixed, posted prices for NT service to FERC's load-ratio share (footnote 32)?

<u>Answer</u>: No. Footnote 32 is intended to suggest a potential solution to what some might view as rate pancakes that could result from a customer paying both a network charge and a charge for a long-term IWR pair. The idea is that the billing determinant associated with the network rate could be reduced by the reserved capacity associated with an IWR transaction used to serve load. The specific design of company rate(s) for each transmission owner, whether based upon load-ratio share or other, may vary among transmission owners, as it does today. These are details that would need further work after Decision Point 2.

(13) **<u>Question</u>:** Is it legal for BPA to charge its transmission customers for "lost revenues" incurred by other transmission owners (p. 33)? Is it consistent with current FERC pricing policy for jurisdictional transmission providers to charge their transmission customers for revenues lost by other providers?

<u>Answer</u>: The first question is one that should be addressed to BPA. The concept of having some mechanism to replace lost revenues is not novel and was included in RTO West Stage 1 and Stage 2 filings submitted to FERC. It would not be out of the ordinary for a transmission owner's rates to reflect the costs of services purchased by the transmission owner to enable it to offer transmission service. A mechanism to replace lost revenues could be part of the overall package that allows Grid West to be implemented – a component of purchasing from Grid West the service of managing the regional transmission system on an integrated basis.

(14) **<u>Question</u>:** What are the differences between "accept all schedules and manage congestion through redispatch" and "issue service rights up to system capability" (Attachment 1)? Is there no redispatch included in the definition of "system capability"?

<u>Answer</u>: In a regime that will "accept all schedules and manage congestion through redispatch," transmission rights are not required to schedule. Instead, the user is charged an explicit congestion charge that is based on the cost of redispatching in a day-ahead energy market so that the schedule can be accommodated. Under Grid West there will be no day-ahead energy market and every schedule must be accompanied by a corresponding physical transmission right. The issuance of transmission rights will be based on the physical capability of the transmission system; therefore schedules are only accepted up to the physical capability of the "wires." Today, some redispatch is done to enable existing rights, e.g., redispatch associated with network service. That amount of redispatch is expected to continue.

Section B.2 – Questions from Paul Whiting

(15) **<u>Question</u>:** I do not completely understand how expansion costs are to be handled. It is clear that the requestor will pay for the embedded cost for the expansion that is built and that they use. However, I assume any expansion built will exceed the requested service by some significant amount. How would "Lost Revenue" be calculated in this case as Grid West would sell the new transmission? Would any of this balance be seen as excess capacity not subject to Lost Revenue demands? Would the capacity built beyond the request then be subsidized by the Lost Revenues? Or, would future expansion be limited in size to the requests?

<u>Answer</u>: The Pricing Work Group has not specifically discussed these questions, but the concept of "lost revenues" as used by the Pricing Work Group has been limited to *existing facilities* and revenues related to *past* service, rather than service that is granted from new construction in the future. This question seems to be getting at how revenue requirement for new construction that exceeds capacity required for a specific service request will be recovered. See the answer to Pricing Seminar Question 27 (Section A).

(16) **<u>Question</u>:** The pricing mechanism set up now has revenues collected first going to cover Lost Revenues. Excess revenues are then spread back to the utilities on a use basis. The theory being the utilities could then adjust embedded cost recovery down. I would prefer to see these funds first used to offset Grid West operating costs and result in reduced Grid West operating charges. This cost relief to the consumer would be more immediate and sure to the consumer. The utilities would still be recovering their embedded costs. Was this approach ever considered? Why was it rejected if it was considered?

<u>Answer</u>: Yes, the Pricing Work Group did discuss the possibility that if Grid West's sales of new transmission service generated *more* revenue that needed to replace lost revenues, the excess could be used to reduce the Grid Management Charge. As explained in the answer to Pricing Seminar Question 33 (Section A), several members of the Pricing Work Group urged that we maintain clear distinctions between costs related to Grid West's operating and development expenses and costs related to transmission owners' revenue requirements. This was the reason that the Pricing Work Group did not propose that surplus AFC sales revenues be used to reduce the Grid Management Charge, but this approach could be revisited. Your understanding of the allocation of excess revenues is incorrect, however. Excess revenues are to be spread back to transmission owners based on revenue requirement (the ratio of each owner's transmission revenue requirement to the aggregate revenue requirement for all transmission owners).

(17) **<u>Question</u>:** The only opportunity for increased revenue from switching from the current system operating system to a flow-based system comes now as the operation basis changes. Will this extra capacity be documented or will it gradually become part base transmission capacity subject to recovering embedded cost? Will there be opportunities in the future to add to this capacity that is not subject to cost recovery during future expansions?

<u>Answer</u>: The Pricing Work Group has not addressed the question of whether it will be possible to document how much additional capacity becomes available for future use through Grid West's flow-based methodology. In addition, the Pricing Work Group has not concluded that the only opportunity for increased revenue results from switching from the current operating approach to a flow-based system. These are areas in which input from the TSLG and Risk/Reward Work Groups would be helpful. The Pricing Work Group's proposals for pricing and cost recovery do make a clear distinction between cost recovery for existing facilities versus cost recovery for expansions or upgrades. The Pricing Work Group did not discuss the possibility of folding part of the current system's costs into future expansions, but the Pricing Work Group assumed implicitly that all system capacity (existing and new) should contribute to recovery of embedded costs – in other words, there was no intent that some capacity (even if it had been latent until Grid West began operations) would be "exempt" from cost recovery.

Section B.3 – Questions from Linc Wolverton on behalf of ICNU

Executive Summary

(18) **Question:** On page 1, line 2. Do these "proposals described" need buyoff by the RRG, the membership, or are they being held for future Independent Board decision without RRG or membership buyoff?

Answer: The pricing proposals for Grid West, as well as all of the other elements of the Grid West package for Decision Point 2 will be presented to the RRG and membership for their evaluation at Decision Point 2. The package will not be presented to the Grid West independent Board unless, in view of all elements of the package, there is sufficient support to continue Grid West development after Decision Point 2. See the answer to Pricing Seminar Question 34(Section A).

Pricing and Cost Recovery

(19) **Question:** On page 8, paragraph beginning "The potential…" "Some long-term point-to-point…may be discontinued if Grid West can provide comparable service…" What does this mean? Please provide some examples. Can this occur before normal contract expiration? If so, isn't the result to have cost shifts?

Answer: In the Pricing Work Group's discussions on this topic, the most commonly cited possibility was a "daisy chain" of contracts that enables a customer to move power across multiple transmission owners' systems (paying cumulative rates for each system used). The Pricing Work Group did not obtain or review data concerning the particular parties to long-term transmission agreements or how these agreements are used (or whether they are used in combination with other transmission agreements), so the Pricing Work Group is not in a position to provide any actual examples.

The reference to "comparable service" was intended to mean that if a party using multiple wheeling contracts to complete a particular transaction could allow the contracts to expire and substitute a single injection-withdrawal pair from Grid West at lower cost, then, because Grid West introduces this possibility, some parties may be in a position to take advantage of it (and they would not have had this option in the absence of Grid West). The Pricing Work Group did *not* expect that this could happen before normal contract expiration (no one in the Pricing Work Group thought that transmission customers have unilateral rights to terminate transmission agreements before their expiration dates). At least on NorthWestern's system, however, there are some wheeling customers who buy transmission service from NorthWestern in one-year increments, and so it would only take one year for these contracts to expire.

The Pricing Work Group has tried to structure the proposal elements to minimize potential cost-shifts, and that is one of the reasons that transmission owners would *not* be permitted to allow long-term contracts to use each others' systems to expire (to the extent the contacts are needed to fulfill load service obligations).

(20) **<u>Question</u>:** As I understand the Reconfiguration Service, existing transmission-rights holders can offer their rights into the market. Presumably, they can offer (non-flexibility) rights and buy them back or have an agent buy them back on their behalf. If such a transaction takes place—an offer and a buyback—the rights holder no longer pays the tariff charges or losses associated with their existing contracts. Instead, they pay the auction clearing price and Grid West (scaled) marginal losses. Is my understanding correct?

<u>Answer</u>: The Pricing Work Group's understanding is that if a transmission customer offers its existing rights into the RCS, this will ***NOT*** relieve the transmission customer of its obligations to the original transmission provider that granted those pre-existing rights. Instead, offering rights into the RCS would allow a transmission customer to recoup some of the costs it incurred to obtain those rights, in those instances in which the customer does not need to use the rights.

To illustrate with a simple example: Customer A has 10-year firm rights on Utility B's system to wheel up to 100 MW of power from point X to point Y. In the month of June, Customer A does not anticipate using its rights. Customer A can offer into the RCS market the 100 MW of X to Y (assuming the underlying contract permits resale or reassignment) for the month of June (and can also offer the rights subject to a minimum bid, if it wishes). Customer A will have to continue to pay Utility B for the X to Y right, whether or not the one-month segment that Customer A offers into the RCS is sold. If the right to move power from X to Y for the month of June is sold in the RCS, then Customer A will receive the applicable clearing price for that right, as long as the clearing price meets or exceeds Customer A's minimum price (if any).

Given this, it should not benefit the customer to buy back its own rights in the RCS, because the customer would still owe its usual payments to the "legacy" transmission provider and it would only pay itself for the purchase of the right in the RCS. The Pricing Work Group has not discussed how losses would be treated in this kind of transaction.

It also might be worthwhile to consult the TSLG about whether it makes sense to presume that in releasing rights into the RCS one can be assured of the ability to repurchase them. The TSLG papers describe the RCS auction mechanism as designed to award the aggregate set of IWRs that maximizes revenues. The papers also indicate that many different IWR sets might depend on common constraints. So it may not be the case that the customer offering rights would automatically be the successful bidder in seeking to repurchase the capacity available from the release.

(21) **<u>Question</u>:** In the lost-revenues analysis, has any reckoning been made of potential transmission-rate lost revenues due to an RCS sell-buyback arrangement as described in No. 3 above? Has any reckoning made of the reduced real power losses in such a transaction?

<u>Answer</u>: No, the Pricing Work Group did not discuss these concepts.

(22) **<u>Question</u>:** Are losses to the TOs deriving from real power losses anticipated to be included in lost revenues? If so, how will the value of power be figured?

<u>Answer</u>: The Pricing Work Group has not discussed the concept of lost revenue related to real power losses.

(23) **<u>Question</u>:** On page 8, paragraph beginning "Of this $1.8 billion…" What is the basis for the "conservative estimate that Grid West short term sales would generate at least half of the 2003 revenues?" Are these sales all nonfirm sales? Don't proceeds of the RCS auction go to those offering up segments and not Grid West?

<u>Answer</u>: Concerning the basis for the "conservative estimate," please see the answer to written Question 2 (Section B.1). As explained in the answer to Pricing Seminar Question 1 (Section A), the RCS will be the mechanism through which both released rights and uncommitted system capacity (AFC) are sold. Revenues from AFC sales will be paid to Grid West, and Grid West will in turn allocate these revenues to the transmission owners. The 2003 revenue figures noted on page 8 of the white paper are combined short-term and non-firm sales revenues.

(24) **<u>Question</u>:** On page 9, paragraph beginning "Estimating potential revenue…" It would appear that all the Northwestern contracts can be converted to Grid West service at the end of the first year and cause, potentially, revenue loss to Northwestern? Is this true? What is the estimate of the revenue loss? Does that revenue loss include reductions in real-power loss obligations of the transmission user? Is that part of page 8's "short-term and non-firm service" payments of $100 million? It appears also, based on the sharing method proposed later in the document that "lost revenue" recovery would become a "replacement revenue" uplift charge if the RCS did not produce enough revenues, true?

<u>Answer</u>: It is not true that "all NorthWestern contracts" could be converted to Grid West service at the end of the first year. There are network service contracts on the NorthWestern system that do not expire within one year. Also, to the extent that some point-to-point contracts on NorthWestern's system expire, this does not necessarily translate into a certain revenue loss for NorthWestern. If the expired contracts were replaced with analogous service solely on the NorthWestern system, then the charges for the new service would be essentially the same as they are today and so there would not necessarily be a net revenue loss. If the current point-to-point service on NorthWestern's system were replaced with multisystem rights granted by Grid West at a nonpancaked rate, then there would likely be a net loss in revenue associated with that service. NorthWestern has estimated the annual revenue associated with its one-year point-to-point contracts to be approximately $8 million dollars, but to the extent Grid West sells new long-term rights to replace the expired contracts (even if these rights are multisystem rights), NorthWestern would get a portion of the resulting revenues.

None of the estimates of lost revenue include revenues related to real power losses.

Grid West would not necessarily need to rely on replacement revenues if the RCS does not produce enough revenue to offset lost revenues. To the extent Grid West is able to sell new long-term service from existing capacity (both capacity that is currently uncommitted as well as capacity that opens up due to long-term contracts that expire), then the resulting long-term sales revenues would be added to RCS revenues and allocated to the transmission owners. It is only if Grid West's *combined* long-term and RCS (short-term) revenues are insufficient to fully make up lost revenues that Grid West would need replacement revenues.

(25) **Question:** Section 2.2 table definition for AFC. Are TRM and CBM needs intentionally omitted from the estimates of AFC?

Answer: The Pricing Work Group's definition of AFC in the table in Section 2.2 of the pricing white paper was intended to track with the definition of AFC established by the TSLG. It may be helpful to consult the TSLG for further information about whether TRM and CBM are included or excluded from the calculation of AFC.

(26) **Question:** On page 16, paragraph beginning "Because through and export…" The PWG says that it "does not believe it is necessary or appropriate to propose a separate, additional charge for exports, and has not done so." For new long-term rights under each of Options 1, 2 and 3, does this mean that a LT right across the intertie would have, in BPA's case, intertie charges as well as network charges? If not, have the cost shifts and power-cost changes for the Northwest been estimated? Is the answer the same for Puget and PGE, which also have segmented rates?

Answer: As noted in the answers to Pricing Seminar Questions 22 and 23 (Section A), neither BPA nor the Pricing Work Group has ruled out the possibility that a transmission owner may, within the company rate approach, continue rate segmentation for use of different facilities on their systems. This possibility was also noted in footnote 23 of the pricing white paper.

(27) **Question:** On page 17, paragraph beginning "First of all...." First of all, the problems and opportunities are a compilation of problems not an agreed upon list. Second, is there any estimate that "<u>on most parts of the system</u> there is more demand for new service than existing facilities can accommodate?"

Answer: The statement that "on most parts of the system there is more demand for new service than existing facilities can accommodate" was based on the experience of members of the Pricing Work Group that many transmission owners are currently unable to grant new long-term service from their existing facilities and statements in TSLG presentations and materials that the TSLG expects that most requests for new long-term service would require upgrades or expansions because of the lack of available long-term capacity. The Pricing Work Group did not develop any estimates related to how likely new long-term service requests were to require upgrades or expansion.

(28) **<u>Question</u>:** On page 19, paragraph beginning on previous page. "Grid West will oversee the process of upgrading or expanding the system as necessary to meet the new service request." What does "oversee" mean? What authority will it exercise (besides coordination)? If a party wants to do something different from what a regional plan includes, does Grid West have the authority to stop it in this oversight role?

<u>Answer</u>: The Pricing Work Group did not have responsibility for developing proposals related to system planning and expansion. The TSLG has posted a draft paper addressing the Grid West planning and expansion process. The Pricing Work Group chose the word "oversee" because the Grid West planning and expansion process have not yet been worked out in detail, but the Regional Proposal expressed the expectation that the planning and expansion process for Grid West would be generally consistent with the process proposed in the RTO West Stage 2 filing.

(29) **<u>Question</u>:** On page 20, the options. Was the option of averaging the rates of the injection and withdrawal points considered? If so, why was it rejected?

<u>Answer</u>: Yes, the Pricing Work Group considered this option. See the answer to Pricing Seminar Question 6 (Section A).

(30) **<u>Question</u>:** Option 2 appears to make BPA the likely destination point for most withdrawals because of its lower rates and its proximity to most loads, but the revenue redistribution does not seem to jibe with the responsibility imposed upon the BPA system to provide service reliably to this transmission. The revenue redistribution appears to favor the high-cost systems—particularly for maintaining reliability. This appears to be a mismatch in cost responsibility versus revenue allocation?

<u>Answer</u>: The Pricing Work Group recognizes that there are some valid concerns with respect to possible incentives to specify particular systems as injection or withdrawal points to obtain favorable company rates. See, for example, footnote 24 of the pricing white paper. The reference to Option 2 is confusing, however, given that if a transaction had an injection point on a higher-cost system, it would not matter that the withdrawal points was on a lower-cost system (such as the BPA system), given that the rate for the IWR would be the *higher* of the rate for the injection system or the withdrawal system. There would be incentives to choose withdrawal points on low-cost systems under Option 1, but it is also true that Grid West's ability to grant IWRs, which are physical rights, on any given system is limited to what the system can support, so even if parties prefer to specify low-cost systems as their withdrawal points, there will be a physical limit to their ability to do so.

Moreover, the Pricing Work Group did not understand that a withdrawal point or an injection point would necessarily dictate entirely the impact that a given IWR has on the system. In other words, the Pricing Work Group did not assume that a right that terminates on the BPA system would necessarily "use" more of the BPA system (on a flow basis) than an IWR that terminates on some other transmission provider's system. The Pricing Work Group felt that the most equitable way to handle the economic risks and benefits for transmission owners joining Grid West was to develop approaches that recognized that all transmission owners' systems contribute to the network's capabilities and all transmission owners should be "kept whole" (from a revenue recovery standpoint) in exchange for making their systems available to all customers on a more integrated basis.

(31) **Question:** Regarding Option 3, does the System Wide Averaging eliminate segment charges, such as the eastern or southern Intertie charges on BPA, PGE and Puget? If Option 3 were shown to bring about significant cost shifts, would that finding be sufficient to eliminate it from the list? Same question, but if it brought about significant power cost shifts?

Answer: The Pricing Work Group did not develop Option 3 to the level of detail this question requires. The Pricing Work Group did not discuss whether Option 3 would necessarily require that southern Intertie costs be rolled into the system average, or if instead there could be some forms of segmentation within Option 3. The Pricing Work Group recognizes that all the options involve tradeoffs among multiple objectives, and that how different parties view those tradeoffs will affect their preferences among the four options presented. The Pricing Work Group did not discuss the issue of power cost shifts at all. Discussions of potential cost-shifting centered on costs for transmission service.

(32) **Question:** Regarding Option 4, how can you have an auction when there may not be any common services and upgrades may be required? Example, a request for service from 2007 to 2012 and another for 2013 to 2018. A service from A to B from 2007 to 2012 and from C to D for 2009 through 2020.

- How do different upgrade requirements for different services fit into the auction method?
- Does Grid West estimate load growth of existing customers as a demand for transmission calculated in the auction?
- Does Grid West assume the upgrade responsibility as a result of the auction, even if auction revenues are insufficient to pay for upgrades? That is, who pays for (or receives the benefits of) the errors in forecasting?
- If this is not for upgrades (in part or in whole) and there is no AFC available, as indicated earlier, then why is it even a serious candidate?

Answer: The auction (Option 4) is proposed as an alternative pricing mechanism for long-term service that uses existing transmission capacity. Therefore, this approach would not apply when system upgrades are involved. In the first example above, two different requests for service, *e.g.*, 2007 - 2012 and 2013 - 2018, an auction could be used: (1) by extending the RCS to cover five year periods of time; (2) by calling for a competition, once the requests are made to Grid West; and, (3) by holding an "open season" for capacity during these time periods. Other option mechanisms could be explored as well.

In response to the sub-questions above:

- Q. How do different upgrade requirements for different services fit into the auction method?

  A. The auction option is not proposed for requests that require expansion. Requests that require expansion would be priced using the "or" pricing policy.

- Q. Does Grid West estimate load growth of existing customers as a demand for transmission calculated in the auction?

  A. The Pricing Work Group concluded that most customers use network service to cover load growth. While the Pricing Work Group's did not directly address which entity would be responsible for estimating load growth, the work group anticipated that these customers will retain their legacy network contracts and as a result, will pay that applicable rate under these contracts for service to cover load growth.

- Q. Does Grid West assume the upgrade responsibility as a result of the auction, even if auction revenues are insufficient to pay for upgrades? That is, who pays for (or receives the benefits of) the errors in forecasting?

  A. The Regional Proposal anticipated Grid West would have a significant role in transmission planning and expansion. If expansion is required, Grid West would be involved in evaluating the need for and benefits from an upgrade or expansion, as well as estimating the costs associated with a range expansion options or a particular solution. The auction is not proposed for requests that require upgrades or expansion.

- Q. If this is not for upgrades (in part of in whole) and there is not AFC available, as indicated earlier, then why is it even a serious candidate?

  A. The Pricing Work Group developed four options to be considered for pricing existing AFC that is surplus to existing needs. Three of the options are cost-based and one is effectively an extension of the RCS auction mechanism. There are different opinions as to which of these options is the best solution or "a serious candidate" for pricing AFC.

(33) **<u>Question</u>:** Regarding Page 26, paragraph beginning "The TSLG…" The statement is made that "if a transmission customer wishes to shift administration of its legacy service to Grid West…, this voluntary transition would be possible." If the shift were for Northwestern, where all customers have potential open-access rights, wouldn't this entail an extraordinary cost for setting up a billing system for hundreds or thousands of customers? Is the cost of that billing system being figured into the cost of Grid West? If not, this offer should be dropped?

<u>Answer</u>: The statement on page 26 of the pricing white paper was referring to customers with *existing ("legacy") transmission agreements*. If NorthWestern currently must manage billing to thousands of transmission customers, then presumably the capability already exists. If not, then all of the potential open-access customers to which this question refers would not be covered by the statement in the white paper, because the white paper's statement was intended to refer to those parties that currently receive long-term transmission service under an OATT service agreement or a pre-OATT service agreement.

(34) **Question:** Regarding page 28, paragraph beginning "Grid West will determine…" Are there any proposed standards for such determination? If a utility believes that the market will provide a resource or a demand-side reduction, but such a resource is not in the plan, must such a possibility be included before the benefits of a transmission upgrade are calculated? For example, if Grid West says that Snohomish gets 10 percent of the benefit of a transmission upgrade, but Snohomish says that it expects a CT or cogenerator to provide power on the tight side of the constraint and obviate the need for the upgrade, what is Snohomish (or BPA's) right to refuse the allocation?

Answer: The white paper's discussion of the planning and expansion process was intentionally general because details regarding Grid West's planning and expansion proposal have not yet been formulated. Instead, the Regional Proposal indicates an expectation that the planning and expansion process for a new "independent entity" (Grid West) would generally follow along the lines of the proposal developed for the RTO West Stage 2 filing.[6] The Pricing Work Group is unable to provide detailed answers about how the planning and expansion process, or the allocation of resulting costs and benefits, would work.

(35) **Question:** It appears to me that much of the AFC sales activity will occur in the I-5 corridor but the revenues from such sales will be allocated disproportionately to high-cost utilities who have a potentially large lost-revenue account or large per-unit transmission revenue requirements—e.g., PacifiCorp, Montana, Sierra Nevada—instead of the utilities that have AFC in the I-5 corridor. [Sales in the Salt Lake or Las Vegas areas would be

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[6] The Regional Proposal said:

The Platform Group's sense is that most regional parties support the general approach to planning and expansion set forth in the RTO West Stage 2 filing. The regional proposal builds on this approach. It contemplates that the Independent Entity would begin producing annual transmission plans once it becomes operational, expanding on then-existing cooperative regional planning processes.

With respect to expansion, the Independent Entity would begin with the ability to determine the injection/withdrawal rights created by new transmission system construction, and it would also have "backstop" authority to assure that reliability standards and total transmission capacity requirements are met. As described above, the ability of the Independent Entity to exercise "backstop" authority with respect to "chronic, significant, commercial congestion" is subject to the Special Issues List process.

Regional Proposal at 23.

allocate to the utilities there because they are high cost.] Is this a fair understanding of the proposal?

__Answer__: See the answer to written Question 30 (Section B.3).

(36) **__Question__:** On page 35, paragraph beginning "From the Pricing Work Group's…" There is a statement that Grid West does not *have* to use the same form of "company rate approach" for the entire eight-year period. Does this mean that certain utilities or providers, such as the CCA, can drop the company-rate approach as long as a few still maintain it? Does it mean that there could be several different company-rate approaches as modifications are done piecemeal?

__Answer__: The intent of this statement was to recognize that there could be more than one way to fulfill a Bylaws requirement to have a "company rate approach"—that the Bylaws do not mandate that Grid West maintain the *same* (initial) company rate approach for the full eight years, but rather that it could, in less than eight years, transition to some other pricing structure that would still meet the Bylaws' definition of *a* company rate approach. The statement was not intended to suggest that it would be permissible under the current Bylaws language for some transmission providers to stop using a company rate altogether before the end of the minimum eight-year period. The Pricing Work Group also did not intend to suggest that there could be several different "company rate approaches" in effect at the same time. The concept of possible transitions was uniform (all transmission owners moving to a modified company rate approach at once) not piecemeal (different transmission owners implementing different "company rate approaches" at the same time).

Section B.4 – Questions from Nancy Baker on behalf of PPC

The proposal contemplates an uplift charge that would replace transmission owners' lost revenues attributable to the implementation of Grid West. The charge would be imposed either on the basis of scheduled energy or actual energy usage or on share of system peak load.

(37) **__Question__:** Will a transmission provider's schedule of legacy contract rights pay this charge?

__Answer__: The Pricing Work Group has not specified if or how transmission providers with legacy contracts would (or would not) "pass through" charges they incur from Grid West.

(38) **__Question__:** What is the rationale for imposing these costs on legacy contracts when those parties are paying pancaked rates and do not contribute to the revenue shortfall?

__Answer__: The Pricing Work Group's general rationale for the replacement revenue charges was to try to find approaches that would be as equitable as possible and not create unreasonable cost-shifts. An energy-based charge would apply to *all* system users—those taking new service (including short-term service using IWRs obtained in the RCS) as well as transmission owners scheduling use of their systems for native load or other legacy service. The Pricing Work Group included a number of proposal elements intended to minimize the potential need for replacement revenues (such as "mandatory rollover" and allocation of all AFC sales revenues to replace lost revenues). To the extent legacy contracts involving pancaked rates remain in place, there should not be much, if any, revenue shortfall associated with long-term service. In a communal system the actions of some parties may have consequences for others; this is true today and will be in the future, with or without Grid West. The Pricing Work Group would encourage continuing efforts to find the best solutions to the range of challenges associated with future transmission pricing.

(39) **Question:** Has the Committee given thought to the manner in which the under-recoveries of the transmission owners would be ascertained and rolled up into the Grid West rate?

Answer: The Pricing Work Group has not developed any details with respect to ascertaining lost revenues. It has only identified the general concepts described in Section 6.1 of the pricing white paper. The Pricing Work Group has not proposed that under-recoveries would be "rolled up" into the "Grid West rate," but rather that, if necessary, there would be a specific (separate) charge to recover lost revenues remaining after allocating AFC sales revenues. The Pricing Work Group has proposed two methods for assessing these charges—transaction-based (schedules or energy) or load-based (share of system peak).

(40) **Question:** If a non-jurisdictional entity recovers all or a portion of its transmission revenue requirement through the rate of a jurisdictional entity, as would be the case here, FERC will review the transmission revenue requirement of the non-jurisdictional entity using the same standard and scrutiny as it would apply to a jurisdictional entity's transmission revenue requirement. FERC cannot determine whether the jurisdictional entity's rate is just and reasonable without scrutinizing the justness and reasonability of the underlying costs (*i.e.*, the non-jurisdictional entity's transmission revenue requirement). (See *City of Vernon*, FERC Op. No. 479, Apr. 19, 2005.) Has the Committee given thought to the acceptability of its proposal if the above is correct?

Answer: The Pricing Work Group has not discussed the *City of Vernon* opinion.

Section B.5 – Questions from Jim McMorran on behalf of Sierra Pacific Power and Nevada Power

(41) **Question:** What exactly does the Grid Management Charge cover? I believe it is depreciation of any facilities that Grid West acquires, amortization of development costs, financing costs for capital improvements, repayment of funding utilities over time and ongoing O&M.

<u>Answer</u>: Your understanding of what the Grid Management Charge is intended to cover is correct, as long as you would consider start-up costs to be included in the category of "development costs." Also, the Pricing Work Group assumes that your reference to "facilities" is intended include such things as office furniture, computers, building space, etc. Grid West will not own or acquire any facilities for generation, transmission, or distribution of electric energy.

(42) **<u>Question</u>:** What happens with short-term non firm revenue? Probably more of a TSLG question.

<u>Answer</u>: If by "short-term non firm revenue" you mean revenue Grid West earns from accepting post-day-ahead schedule adjustments or new requests on a first-come, first-served basis, then although the Pricing Work Group did not specifically discuss this, the likely expectation would be that it would be treated the same as other revenues from Grid West sales of AFC—that is, included in the "communal bucket" for allocation to the transmission owners.

(43) **<u>Question</u>:** If the revenue replacement charge is necessary and transaction based, would it be charged to a transmission owner's transactions scheduled on its own system?

<u>Answer</u>: The TSLG white paper on scheduling indicates that all use of transmission owners' systems (whether by new customers with IWRs or by transmission owners serving legacy obligations) will be scheduled through Grid West (see TSLG Scheduling & Schedule Adjustments white paper at 3-5). Consequently, a transmission owner's use of its own system would be subject to a transaction-based replacement revenue charge if Grid West were to impose one.